

Public Pension Protection & Modernization

PROTECTING KENTUCKY'S
PUBLIC EMPLOYEES, TEACHERS & RETIREES

May 29, 2008



The Growing Storm

Significant consequences of inaction :

- HB 600 could have saved nearly **\$500 million annually** from state's and local governments' pension system funding obligations.
- Action by July 1 means **county and city governments** get at least \$50 million dollars of immediate relief.
 - Inaction will result in possible loss of jobs and interruptions of critical services.
- Doing nothing could lead to a full **credit rating downgrade**, meaning \$58 million in additional debt service payments.
- Kentucky will experience a record number of **retirements** in '08.
 - Failure to stem “double dipping” will impose significant costs to the state.

The Growing Storm

State leaders agree: [We need pension reform NOW.](#)

Senate President David Williams, *Associated Press* March 7, 2007, *"The government will implode. And the only choices that we will have in future years are to drastically cut these services which our people depend on, or make huge tax increases."*

House Speaker Jody Richards, *Kentucky Tonight* January 7, 2008, *"I think its certainly a tough situation...we are going to have to take action."*

Senate Majority Leader Dan Kelly, *LRC News Release* April 16, 2008, *"The pension issue threatens to bankrupt the state...if we don't act."*

State Sen. Damon Thayer, *www.ThayerForSenate.com* April 8, 2008, *"A failure to act in a quick and decisive manner is intolerable."*

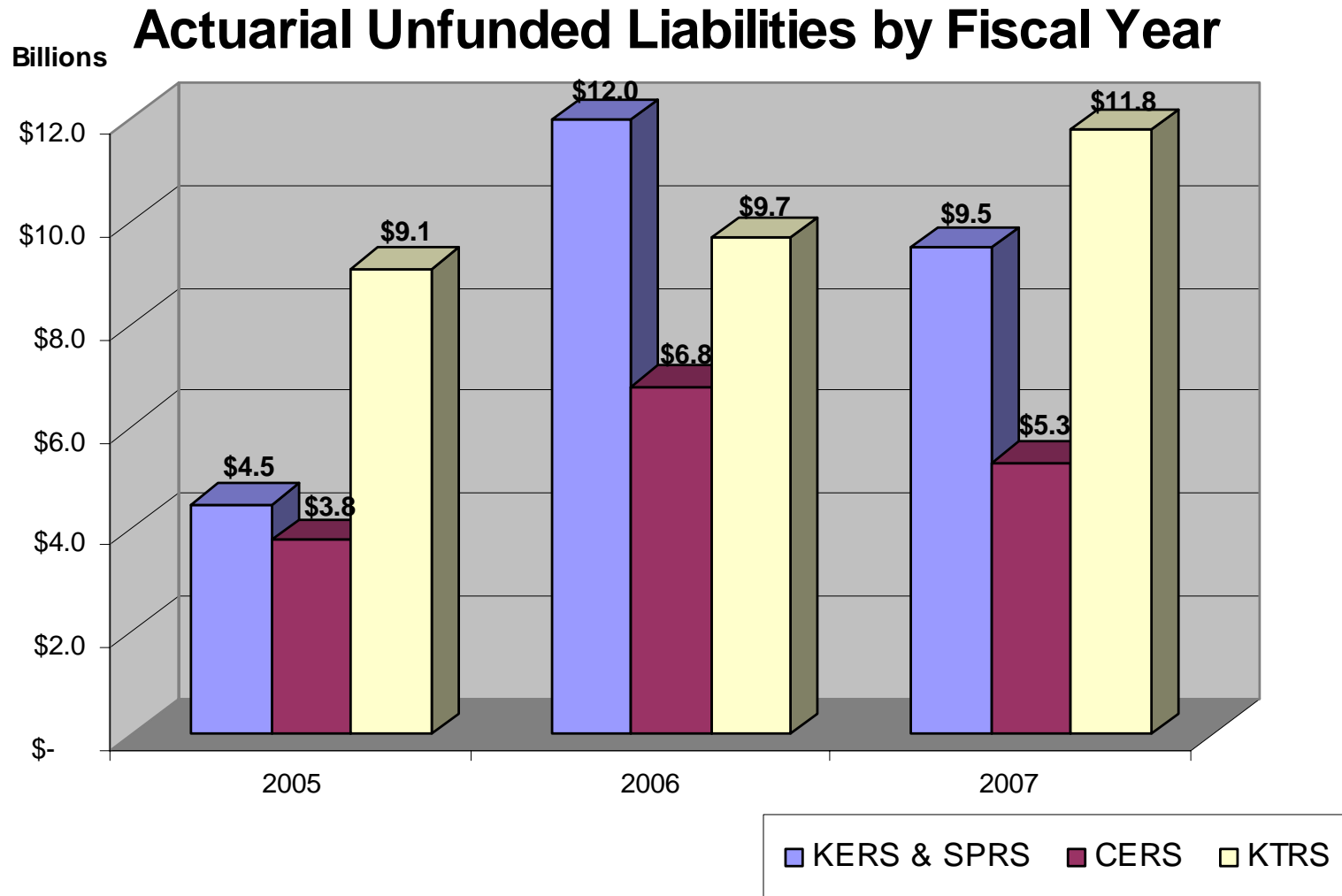
State Rep. Dennis Keene, *The Kentucky Enquirer* May 15, 2008, *"We simply cannot afford to wait another year to pass Kentucky public pension reform legislation. The stakes are much too high."*

Campbell County Judge Steve Pendery, *The Kentucky Post* January 8, 2008, *"We're rapidly approaching cuts to essential services. Something's got to be done."*

Sylvia L. Lovely, CEO of the Kentucky League of Cities, *The Courier Journal* April 17, 2008: *"We are at a point of desperation. We need a fix, we need a solution."*

Dave Adkisson, CEO of the Kentucky Chamber of Commerce, *The Courier Journal, OPED* April 18, 2008, *"Public safety is at risk in our cities, new dollars for education are being eaten up by benefit costs...Surely we can do better in Kentucky."*

The Problem We Inherited

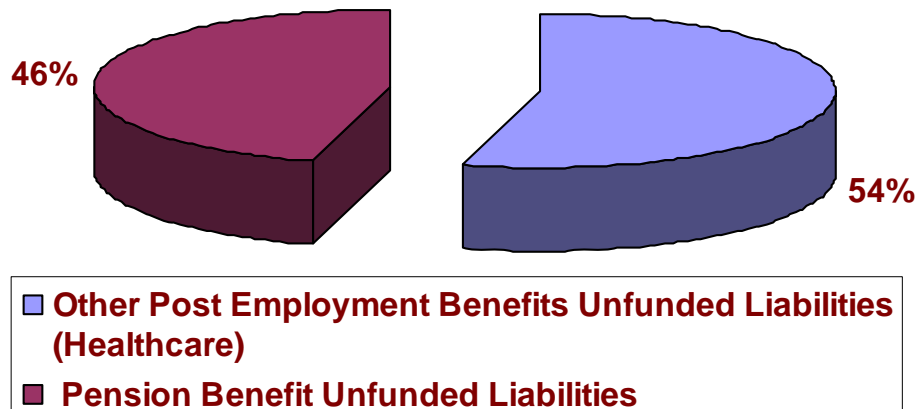


How did this happen?

1. Soaring **health care costs**.
2. Investment **return inadequate** to meet added benefit liabilities.
3. State **under-funding** for 7 of the last 13 years.
4. Benefit **enhancements** made without rigorous cost/benefit analysis.

1. Tackling Health Care Costs

Healthcare as a Percentage of the Retirement Systems' Total Unfunded Liability



To assure quality, affordable and sustainable health insurance coverage, changes must be made to the Kentucky Employee Health Insurance Plan.

- Group Health Insurance Board **bringing all stakeholders to the table** to recommend adjustments in payments and plans.
- **Best Practices Subcommittee** established to help negotiate better contracts.
- State **wellness** programs are being improved and expanded.

Today's Executive Order

- Tackles Issues #2 & 3:
- Creates the **Kentucky Public Pension Working Group**, composed of senior executive branch officials, pension fund directors, employee representatives, and private sector investment experts, will:
 - Conduct an operational and governance review of the systems and recommend new investment benchmarks and strategies for **better investment performance**.
 - Provide recommendations to reach the **actuarially required contribution (ARC) by 2020**, using the benchmarks provided by the Senate.

Today's Executive Order

- The Working Group will also study the issues in dispute during the legislative session that *had not been recommended by the prior administration's Blue Ribbon Commission*, to determine their viability and cost:
 - In which pension system do we locate the classified school employees (bus drivers, janitors, cafeteria workers, etc)?
 - How would we establish a Local Government Employees Retirement System (LGERS), as suggested by the Senate?
 - Should future hires be transferred to a 401(k)-style defined contribution or annuity-type pension plan?
- The Working Group will offer to provide testimony to the Interim State Government Committee, allowing the General Assembly to address these issues in the 2009 Regular Session.

A Special Session?

- Reducing costs to the Systems will require legislative action.
- Today, the Governor met with House and Senate leaders to bring the parties together and facilitate a compromise:
 - Let's deal with the **controversial issues in January**, after sufficient study and discussion. Remember: These issues were NOT recommended by the prior administration's Blue Ribbon Commission.
 - Let's pass legislation in a short, quick special session on all of **those issues where there already is substantial agreement** between the House and Senate.

Issues in Agreement

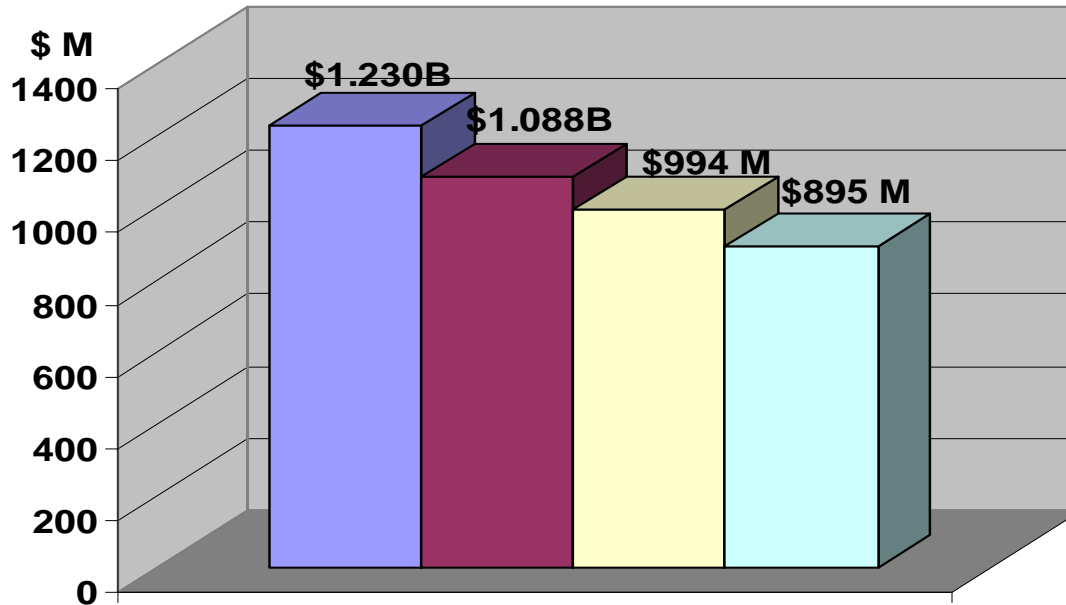
- Modernization of the Kentucky Teachers' Retirement System. The SCS already accepted this section of House Bill 600 **in its entirety.**
- Modernization of the Legislators' and Judicial Retirement Systems. Both sides have already accepted provisions to lower the **COLA to 1.5%** and require future hires to contribute **1% of their salaries** to the health insurance fund.

Issues in Agreement (cont.)

- **Modernization of the Kentucky Retirement Systems:**
 - For **future hires**: extending retirement ages, lowering benefit factors, and penalizing early retirement;
 - Lowering the **COLA** to 1.5%;
 - Reforming the practice of **double-dipping**;
 - Governance reforms —relating to **transparency**, fiduciary duty, and board responsibilities;
 - Requiring all future hires to contribute **1% of their salaries** to a health insurance fund;
 - Reforming practices such as **sick leave**, lump sum payments, and service purchases; and
 - Lowering the **CERS employer contribution rates**.

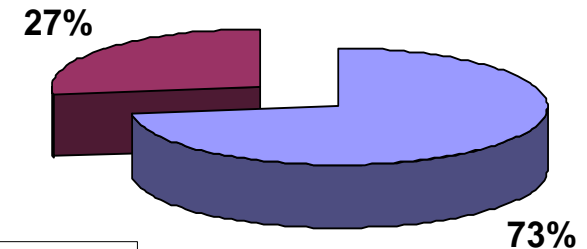
Total Savings for KRS ANNUALLY

Total Annual Savings for KRS \$335 Million/Year Beginning FY '09



- Current Annual State and Local Obligation (Actuarially Required Contribution)
- ...With Proposed Benefit Changes for Future Hires and COLA Adjustment
- ...Plus Changes From 2003 Medical Reform
- ...Plus Investment Savings from Reaching National Average for Investment Returns

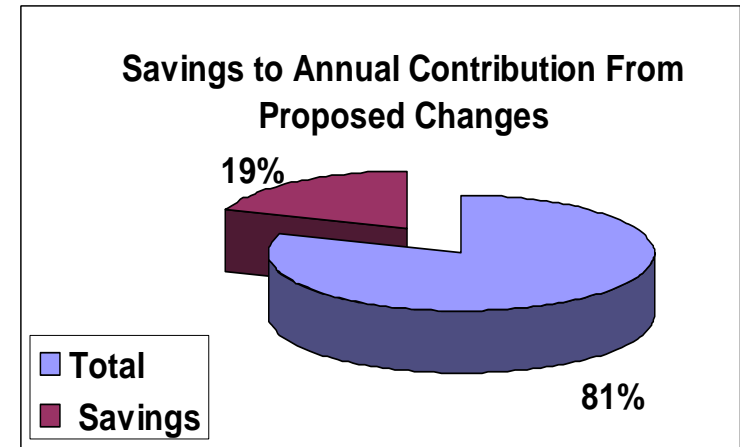
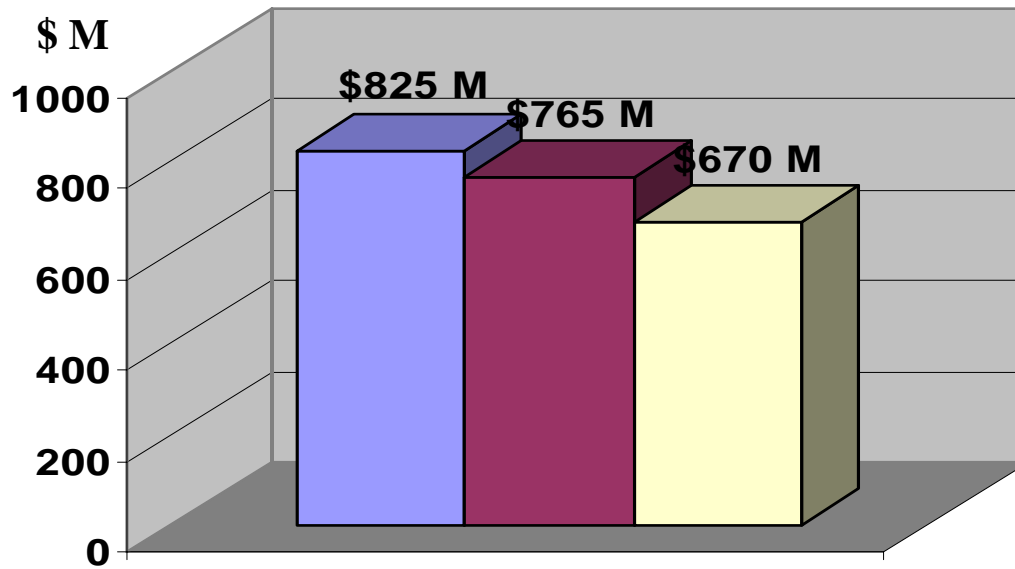
Savings to Annual Contribution From Proposed Changes



- Total
- Savings

Total Savings for KTRS ANNUALLY

Total Annual Savings For KTRS \$155 Million/Year Beginning FY '09



- Current State Obligation (Actuarially Required Contribution)
- ...With Proposed Benefit Changes for Future Hires
- ...Plus Investment Savings from Reaching National Average for Investment Returns

FY 09 Savings for Cities, Counties and School Districts

	CERS Non Haz	CERS Haz
Current Contribution Rate	15.58%	31.99%
<u>Proposed Rate in Draft Plan</u>	<u>13.50%</u>	<u>29.50%</u>
Difference (Savings)	2.08%	2.49%
2009 Estimated Payroll	\$2,122,958,000	\$472,048,803
Estimated Savings	\$44,157,545.12	\$11,754,015.19
TOTAL = \$55,911,560		

Working Group

Members

1. Finance Secretary (Chair)
2. Budget Director (Vice-Chair)
3. Attorney General
4. Secretary of State
5. Auditor
6. State Treasurer
7. Commissioner of Agriculture
8. Personnel Secretary
9. Two appointees of Senate President
10. Two appointees of House Speaker
11. KRS Executive Director
12. KTRS Executive Secretary
13. Reps. of teachers, hazardous and non-hazardous employees
14. Reps. of KACO and KLC
15. Reps. Of KY Chamber and Prichard Committee
16. Five qualified actuaries and/or investment experts.

Subcommittees

1. Investments (Treasurer Hollenbach, Chair)
2. Securities Litigation (General Conway, Chair)
3. CERS Reorganization (Auditor Luallen, Chair)
4. State Funding (Director Lassiter, Chair)
5. Defined Contribution Study (Secretary Jackson, Chair)